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July 30, 2008

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Board of Governors of the Federal Reserve System
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Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW
Washington, DC 20552
ATTN: OTS–2008–0004

Re: BOARD Docket No. R–1314; OTS Docket No. OTS–2008–0004; Unfair or Deceptive Acts or Practices; 73 *Federal Register* 28904; May 19, 2008 (UDAP Proposal)

Ladies and Gentlemen:

The American Bankers Association (ABA) provides these comments on the rule proposed by the Federal Reserve Board (Board), the Office of Thrift Supervision (OTS) and the National Credit Union Administration (NCUA) covering Unfair or Deceptive Acts or Practices (UDAP) involving overdraft protection service fees. ABA brings together banks of all sizes and charters into one association that works to enhance the competitiveness of the nation's banking industry and strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $12.7 trillion in assets and employ over 2 million men and women.

ABA members across the board are concerned about this UDAP Proposal and its possible effect on banks' abilities to safely and soundly exercise their risk-based discretion to pay inadvertent customer overdrafts that are otherwise reasonably avoidable when depositors follow prudent account management practices. ABA has long demonstrated its leadership on this issue by sponsoring the 24-page booklet, *Overdraft Protection: A Guide for Bankers,* that sets forth important principles to consider to guide our members and to benefit our customers. Our membership believes that the banking industry has acted in the best interests of its customers and the payments system by making overdraft accommodation available.

Although the UDAP Proposal covers both credit card practices and overdraft service fees, we address these matters in separate letters to underscore that we believe that overdraft practices have been improperly swept up in the UDAP regulation initiative. Our comments represent the input of banks of all sizes and charters and reflect the strong position of our Board of Directors and our other policy making bodies. We believe that reform in this area should travel a different path.

Summary of Comments

The banking industry has always exercised discretion to cover overdrafts for good customers. Today, banks have developed safe and sound programs that extend this discretionary accommodation to the vast majority of our customers. Bank overdraft accommodation practices are successful because they provide desirable back-up for customer payment decisions, and they are sustainable because people want the bank to recognize that when they inadvertently overdraw their account they can be trusted to make it right and are prepared to pay for the bank's accommodation.

ABA strongly disputes the assertion of the proposal that these overdraft accommodation practices and their associated fees are unfair because the fees cannot be reasonably avoided without elaborate opt-out mechanisms. This errant assertion is belied by long-standing principles of banking law that expect depositors to be responsible for their own account management. In fact, as the banking agencies themselves have publicly recognized and espoused, the best way to avoid overdraft fees is to manage personal bank accounts wisely—keeping track of your paper and electronic transactions and monitoring changes to your balance.

ABA believes that the mainstream practices that banks follow in the area of overdraft accommodation do not merit being a target for the agencies' precedent setting exercise of their self-initiated Federal Trade Commission Act (FTCA) rule-making authority. Banking industry overdraft accommodation practices do not trip the standards that should be applied for determining when banking behavior is unfair under the FTCA, and for that reason alone the proposal should be withdrawn, or certainly not pursued within the UDAP context. Most troubling is the analytical underpinnings of the proposal's assertion that customers cannot be expected to know with perfect certainty their precise account balance at all times and consequently should be absolved from responsibility for managing their accounts or conducting their transactions. This premise is anathema to the fundamental assignment of responsibilities that have been established by federal and state payments law, and its adoption under the authority of UDAP rule-making threatens to impact adversely virtually all banking fees and payment obligations dependent on customer behavior.

The agencies must take special care in establishing appropriate standards for this inaugural exercise of banking agency initiated FTCA Section 18(f)(1) rule-making, need to take special care in establishing appropriate standards to conclude that the banking industry's mainstream overdraft practices are not unfair to customers, and they need to be equally careful to pursue any reform of consumer protection for debit card transactions within the established regulatory framework for electronic transactions, funds availability and account disclosures.

General Background

Americans enjoy the most affordable, efficient, and accessible banking system of any country in the world. Today, customers can open a checking account with a minimal deposit and have access to the entire menu of payment services – at little or no cost. They can write checks, use debit cards to withdraw cash or make purchases, pay bills, and make fund transfers online at any time, day or night, from virtually anywhere in the world. For customers, such an easy and convenient service, however, is not without important responsibilities.

In the best of all worlds, people would only write a check or make an electronic payment when there are sufficient funds in their bank accounts to cover the transaction. Of course, this is not a perfect world. There are also many different ways for consumers to make payments today, which service, while convenient for them, increases the importance of keeping track of what payments they have made and what resources are available to them in their bank accounts to cover those transactions.

Keeping track of transactions is critical to avoiding overdrawing an account. Doing so is part of good financial management and an important responsibility of using any transaction account. Writing transactions in your checkbook or ledger is, of course, the best way to track transactions. This is even more important today with the variety of ways that customers can make transactions.

The Federal Financial Institutions Examination Council (FFIEC) reiterated the importance of personal financial management in the Interagency consumer resource brochure, "Protecting Yourself from Overdraft and Bounced-Check Fees," distributed with a press release that noted "the *best way to avoid* overdraft and bounced-check fees is to manage accounts wisely. That means keeping an up-to-date check register, recording *all electronic* transactions and automatic bill payments, and monitoring account balances carefully." (Emphasis added.) The brochure itself describes *nine* different ways to avoid such fees, the second bullet point of paying special attention to electronic transactions being emphasized in bold print. This brochure was intended to be consumer friendly, and available free on the agencies' websites for downloading so organizations could add their logo for distribution to clients and customers.

The bottom line is that customers are in the best position to know what their actual balance is – only they know what checks they have written, automatic payments they have authorized, and debit card transactions they have approved. Simply put, customers are in control of their finances and can avoid overdraft fees.

However, even if individuals do not keep an accurate, up-to-date record of their transactions and balance, it is easy to check the most recent balance. Customers can – and should – check their transactions and balances often by phone, at the ATM, online, or even using the Internet browser on their phone or other handheld devices. Knowing the balance – and what transactions have been authorized by the customer, but have yet to be processed and are not reflected in that balance – are very important to avoid overdrafts.

Over time, however, customers have sought and appreciated having flexibility against occasional error. This is why banks have traditionally paid overdrafts on a discretionary basis, based on the historical activity of the account and the likelihood that the accountholder will cover the overdraft. Today's "bounce protection" or overdraft accommodation programs are basically the latest, customer-driven innovation of this traditional practice. The primary difference is that many of the more recent overdraft protection practices rely on ***automated*** systems. The advantage of the automation of the historical practice of paying overdrafts on a discretionary basis is that it reduces costs associated with case-by-case assessment and manual intervention and promotes consistent treatment of customers.

Customers who find it challenging to manage their accounts and avoid overdrafts have other options available to them. Many avoid overdrafts by maintaining a cushion in the account to cover transactions they may have forgotten about or not written down in the checkbook. Others, for example, arrange for overdrafts to be covered by automatic transfers from a savings account or to a credit card account. Still others establish a line of credit to cover overdrafts. In contrast to simple overdraft accommodation provided as a courtesy by banks, these are legal agreements where the bank is *obligated* to pay overdrafts and customers must complete applications and be subject to the bank's underwriting standards to quality. Customers may also arrange to have the bank send them electronically daily notices of their balances and alerts warning them when their balance falls below a set amount. What works best for one customer may not work as well for another. And room must be preserved for future innovation to meet changing customer demands or to take advantage of new technologies.

Overdraft protection is an important service for our customers, and we believe customers should understand the process, the responsibilities to track deposits and withdrawals, and any fees associated with overdrafts and options to avoid them. Banks can and do provide convenient access to account information today to help customers manage their financial flows, but ultimately it is consumers who are in the best position to track and manage their accounts and choose among the overdraft options available to them.

Customers value depository institutions paying their overdrafts.

Ever since banks first introduced transaction accounts, the issue of how to deal with overdrafts was front and center. Obviously, the management and control of deposits and withdrawals are in the hands of the customer.

In most cases, the customer initiating a payment transaction wants to complete it and appreciates the bank paying it, even if there are insufficient funds. Indeed, ABA's recent survey found that of the 20 percent of consumers who had paid an overdraft fee in the last year, 85 percent were glad their bank did so.[1] The Center For Responsible Lending in its January 2007 survey showed a similar attitude among consumers: Over 92 percent, when asked, said they would like the bank to pay it and were willing to pay something for it. (See attached.) It is also typically the case that even with the bank's fee, the costs of rejecting the transaction and returning the check – including the inconvenience, embarrassment, and fees charged by the merchant or payment recipient – is greater.

Today, with so many transactions taking place, overdraft protection practices are automated with specific criteria and limits on the coverage. Usually, the amount paid is between $100 and $500, depending on account history, under certain circumstances. Examples of typical criteria for eligibility for the service include:

- Minimum monthly deposit;
- Periodic direct deposit;
- No delinquencies with the bank;
- Age of account;
- Average balance; and
- Maximum number of overdrafts over a certain period of time.

The advantages of the automation over the historical practice of paying overdrafts on a discretionary basis are that it reduces costs associated with case-by-case assessment manual intervention and promotes consistent treatment for all customers.

Banks explain to customers that the bank ***may*** honor overdrafts. That does not nullify the fact that *knowingly* making a payment without having available funds to cover it is not only a dangerous financial practice, it is illegal.

Nevertheless, customers value banks' practice of paying overdrafts. Indeed, they expect it. They value the ability to avoid the embarrassment, hassle, costs and other adverse consequences of having a check bounce or transaction denied. Whether made by check or electronically, returning a payment to a merchant, mortgage company, or credit card company, usually means the customer pays additional fees charged by the person receiving the payment. Through overdraft accommodation services, customers avoid the inconvenience of having to resolve the issue and arrange a second payment. They also escape the risk of having adverse information reported to a credit bureau or "bad check" database. Moreover, inasmuch as the customer pays a fee whether the bank pays the item or returns it unpaid, customers typically appreciate the depository institution paying items when there are insufficient funds.

Customers also value having debit card point of sale transactions approved even when there are insufficient funds. For example, many consumers would rather their depository institution authorize the debit transaction than face the consequences of

[1] See ABA Overdraft Fee Study, Ipsos U.S. Express Telephone Omnibus, (July 11-13, 2008).

not being able to pay for a meal they have just consumed or the groceries that have been rung up and bagged.

Customers understand the timing of transactions and how to manage within the overdraft accommodations provided by the bank. For example, some customers are aware of and avail themselves of the fact that even with debit card transactions, there is often some window of opportunity to deposit funds ***after*** a transaction is made. For example, some people in some situations may be able to make a purchase in the morning with their debit card – uncertain about their available funds at that time – and transfer or deposit money into their account before the books are closed for that day to cover the shortfall.

Customers have many options to avoid overdraft fees.

It is important to emphasize that customers have options to avoid overdraft fees. As discussed earlier, customers can avoid overdrawing their accounts by keeping track of their transactions, which banks are employing new technologies to make easier and easier to do.

Customers can check account activity and balances online or by phone. Even if they do not keep an accurate up-to-date record, customers can check their available balance just prior to a transaction by phone, at the ATM, or using the Internet browser on their handheld device. They can also arrange to have overdrafts paid through an overdraft line of credit, credit card, or savings account. Depending on the individual customer's behavior and habits, these latter options can be less costly than overdraft fees, but customers must meet underwriting standards of the bank to qualify (which includes a credit check) or have a savings account at the bank.

Many consumers avoid overdrafts by keeping a cushion of funds. In addition, depository institutions commonly permit customers to opt out of having overdrafts authorized or paid. However, they usually still have to pay a bank overdraft fee as well as any merchant or payee's fee for any returned item. In addition, the option generally means that *all* non-sufficient funds transactions, not selected types of transactions, such as debit card transactions, will be returned or denied.

Depository institutions will often waive the fee for an initial or occasional overdraft. After the first incident, the consumer is then aware that debit card transactions may cause an overdraft and can take appropriate steps to avoid them. Of course, customers dissatisfied with their bank's services have many other banks to choose from in our very competitive industry.

Banks follow responsible overdraft protection practices.

As automated overdraft accommodation programs became more prevalent and people's experiences with them increased, questions and concerns arose about how some of these promoted accommodation programs work and how best to avoid overdraft fees.

ABA responded to these concerns in a March 21, 2003, letter sent to all ABA members from Ken Fergeson, the ABA Chairman-Elect at the time. The letter advised ABA members to exercise caution with regard to overdraft practices and offered specific suggestions. Subsequently, ABA partnered with Alex Sheshunoff Management to publish and distribute to all ABA members more extensive information, the 24-page *Overdraft Protection: A Guide for Bankers*.

These documents drew banker attention to suggestions that depository institutions:

- Disclose costs and terms in the agreement fully and conspicuously;
- Make clear that the depository institution is not promising to pay items; Avoid encouraging customers in marketing materials, advertising, and communications, to overdraw;
- Monitor accounts for frequent use of the service and take appropriate actions in these situations;
- Inform customers of other ways to handle overdrafts, such as lines of credit and automatic transfers; and
- Proactively offer an opt-out to customers.

In 2005, the banking agencies adopted their *Overdraft Protection Program Guidance* (Guidance) that reflects many of the industry's recommendations. The agencies' Guidance addresses legal and safety and soundness issues and also includes best practices. Specifically, the Guidance recommends as best practices that depository institutions:

- avoid promoting overdrafts;
- fairly represent overdraft protection programs and alternatives;
- train staff to explain program features and choices;
- clearly explain the discretionary nature of the program;
- clearly disclose program fees;
- demonstrate when multiple fees will be charged;
- explain impact of transaction clearing polices; and
- illustrate the types of transactions covered including card transactions, preauthorized automatic debits, telephone-initiated transfers, and other electronic transfers.

The Guidance offers specific best practices related to program features and operations. For example, depository institutions should:

- provide election or opt-out of service;
- alert consumers before a transaction triggers any fees where feasible, e.g., at the teller window;
- prominently distinguish balances from overdraft protection funds availability;
- promptly notify consumers of overdraft protection program usage each time used;

- consider daily limits on consumers' costs;
- monitor overdraft protection program usages; and
- fairly report program usage.

One issue of concern has been repetitive use of overdraft accommodations by customers. Banks do, as expected in the Guidance, monitor excessive use, and notify customers of other available options for managing their accounts. The Guidance also requires suspension of services when "there is a lack of timely repayment of an overdraft." Bankers follow these practices closely, with many institutions suspending overdraft accommodation when an outstanding balance exceeds 30 days. This means customers who have difficulty managing their account and avoiding overdrafts will not get into debt for any extended period of time or fall into a "cycle of debt" due to overdrafts.

The Federal Reserve Board went further to address concerns about customers' understanding of the cost of overdrafts by amending Regulation DD (Truth in Savings). Specifically, the regulation requires depository institutions that "promote" overdraft protection to disclose in periodic statements the total dollar amount of fees for paying overdrafts and the total dollar amount for fees for returning items unpaid. These totals would have to be provided for the statement period and *for calendar year to date.* All depository institutions would also have to specify to customers the categories of transactions for which an overdraft fee may be imposed, including, for example, ATM withdrawals and point-of-sale debit card transactions.

We believe that the industry's initiative, along with the agencies' Guidance and important changes to Regulation DD, have established a set of mainstream practices that characterize successful and beneficial overdraft protection practices. *There has been no evidence provided by the proposing agencies that demonstrates that their supervisory experience with these regulatory standards has been unsuccessful in properly managing UDAP risk in the implementation of overdraft protection programs.* Certainly there is no basis to reverse field now by labeling the thousands of banks that provide this service—and have observed the Interagency Guidance—as engaging in unfair practices just because they have not implemented the elaborate opt-out requirements suggested in this proposal.

LEGAL BACKGROUND

The Board and the OTS have based their proposed rule on Unfair or Deceptive Acts or Practices (UDAP Proposal) on the authority bestowed by the Federal Trade Commission Act Section 18(f)(1), 15 U.S.C. 57a, and the standards for unfairness that Congress codified in 1994 with respect to the FTC's exercise of such authority. We note that the statutory authority of Section 18(f)(1) provides that the Board and OTS "shall prescribe regulations to carry out the purposes of this section, including regulations defining with specificity such unfair or deceptive acts or practices, and containing requirements prescribed for the purpose of preventing such acts or practices."

The current UDAP rule-making will establish the founding principles of unfairness analysis for all banking practices and must be approached with extreme caution to guard against serious adverse unintended consequences for industry operations, customer service value and market innovation with respect to and beyond the particular circumstances covered by the current proposal. While the agencies have relatively recently issued supervisory guidance subscribing to the basic principles applied by the FTC to determine unfairness, this rule-making will elevate those supervisory standards to a regulatory level. Although the Board and OTS have previously adopted the FTC's Credit Practices Rule (Regulation AA), this will be the first exercise of the independent rule-making authority bestowed by FTCA Section 18(f) on the Board and OTS in the more than 30 years of its existence. Its precedent-setting nature cannot be over emphasized, invoking the need for extreme care.

The Board and OTS are, as a legal matter, writing on a blank slate since the standards for unfairness contained in the FTCA (15 U.S.C. 45(n)) are expressly imposed only on the FTC. Despite being added in 1994 at a time when the FTCA already granted the Board and OTS their independent rule-making authority, the unfairness provision of the amended Act is directed only at the FTC[2]. Nevertheless, the Board has previously subscribed to these standards for supervisory purposes and the OTS has acknowledged their applicability as the basis for this proposal.

ABA concurs as a policy matter that the four elements of unfairness recited in 15 U.S.C 45(n) constitutes an appropriate starting point for establishing banking agency UDAP precedent. However, banks were excluded from FTC jurisdiction, and the banking agencies were granted authority in its stead, because there are important distinctions regarding regulatory oversight between the closely supervised banking industry and the unsupervised commercial market that are particularly relevant when developing UDAP precedent for banks. ABA believes that prime among those distinctions is the safety and soundness obligation imposed on banks. Safety and soundness is the operational and supervisory imperative that must be accounted for within any UDAP framework to be constructed by the rule-making banking agencies.

ABA recommends that, at a minimum, safety and soundness considerations be incorporated as part of the countervailing benefits prong of the FTC unfairness test. This would make the test include consideration of countervailing benefits to consumers, to competition and to bank or industry safety and soundness.

This implied extension of the FTC unfairness standards is not the only addition that should be made to the analytical components used by banking agencies in exercising FTCA unfairness rule-making authority. Application of FTC UDAP unfairness standards to banking transactions must also be done with recognition that the payments system is a special franchise that is already heavily regulated and whose

[2] Nothing in section 18(f) expressly requires either the Board or the OTS, when acting on their own initiative, to be myopically focused on the FTC unfairness standards published in 1980 and codified as expressly applicable to the FTC in 1994 under 15 U.S.C. 45(n)—both of which events occurred after the Board and OTS were granted authority to do rule-making under the FTCA and neither of which purport to constrain the 18(f) agencies for rule-making or enforcement purposes.

component parts work in an integrated fashion to achieve operational efficiency, reliability, speed, financial soundness, security and exceptional consumer convenience. FTCA Section 18(f) acknowledges that the banking sector has unique circumstances by expressly providing the Federal Reserve Board with the power to diverge from FTC UDAP rule-making on the basis that applying regulatory standards developed in the commercial market to banks "would seriously conflict with essential monetary and payments systems policies of such Board."

The Expedited Funds Availability Act (EFAA) and its implementing Regulation CC have been the federal baseline for funds availability and the cornerstone for both bank and consumer expectations. They establish when funds from deposits must be available to customers and also firmly recognize that certain holds are necessary and appropriate in order to protect and manage the payment system. In addition, they ensure that bank customers have sufficient information to understand when funds are available by requiring multiple disclosures in multiple locations. The Electronic Funds Transfer Act and its implementing Regulation E assign to the Board the responsibility "to provide a basic framework establishing the rights, liabilities and responsibilities of participants in electronic fund transfer systems." According to the EFTA, "the primary objective of this [law] is the provision of individual consumer rights." As such, both Regulation CC and Regulation E embody precisely the type of payments systems policy that section 18(f) mandates that the Board guard against impairing when developing UDAP rules.

It follows that neither the Board nor the OTS should exercise their UDAP rule-making authority under 18(f) in a manner that undermines monetary or payment systems policies and that in the interests of comity both should include this consideration among their enumerated standards for exercising such authority.

OVERDRAFT ACCOMMODATION FEES ARE NOT UNFAIR

The Board and OTS proposals are based on a premise that "assessing overdraft fees before the consumer has been provided with notice and a reasonable opportunity to opt out of the institution's overdraft service appears to be an unfair act or practice under 15 U.S.C. 45(n) and the standards articulated by the FTC." ABA contests this assertion and believes that the predominant practices by which banks provide overdraft accommodation and assess fees for paying overdraft items are not unfair under standards appropriate under Section 18(f).

In conducting their analysis both the Board and OTS invoke the FTC unfairness standards that derive from the FTC's Unfairness Statement as subsequently codified in 15 U.S.C. 45(n). Succinctly stated, the FTC may not declare an act unfair unless:

(1) It causes or is likely to cause substantial injury to consumers;
(2) The injury is not reasonably avoidable by consumers themselves; and
(3) The injury is not outweighed by countervailing benefits to consumers or to competition.

In addition, the FTC may consider established public policy, but public policy may not serve as the primary basis for its determination that an act or practice is unfair.

Although they cite the FTC Unfairness Statement, as the analysis proceeds the agencies do not explicitly consider either general sources of public policy nor the Section 18(f) mandate covering monetary or payment systems policies. We will treat each of the five elements ABA believes are relevant to a banking agency UDAP unfairness analysis below:

Overdraft accommodation fees are not substantial injuries.

As the Board and FDIC note in their 2004 Interagency Guidance on Unfair or Deceptive Acts or Practices by State-Chartered Banks (Interagency UDAP Guidance), substantial injury usually involves monetary harm and includes situations of a small harm to a large number of people. It is instructive that the FTC Unfairness Statement (adopted as the source of the unfairness portion of the Interagency UDAP Guidance) describes substantial injury in terms more reflective of harmful effects than are present in the overdraft accommodation proposals. For instance, the statement reads, "In most cases a substantial injury involves monetary harm, as ***when sellers coerce consumers*** into purchasing unwanted goods or services or ***when consumers buy defective goods*** or services on credit but are unable to assert against the creditor claims or defenses arising from the transaction. ***Unwarranted health and safety risks*** may also support a finding of unfairness." (Emphasis added.) Charging market rates disclosed at time of contract seem anathema to the label "injury." Although a $7.95 monthly charge to all Orkin customers may be an injury when applied in breach of a termite service contract[3], imposing fees fully disclosed in accordance with the prevailing regulatory scheme and applied pursuant to the express terms of an account agreement cannot fairly be called an "injury."

Fees for covering overdrafts are in the account agreement and new customers are informed of these fees as well as any maintenance fees and non-sufficient funds (NSF) fees at account opening. These disclosures are specifically mandated by Regulation DD (Truth-In-Savings Act) and as a matter of state contract law. Customers understand that it is their responsibility to balance their accounts—and the fees provide both an incentive to do so and a user charge when they inadvertently fail to do so. In other words, customers know in advance what the rules and the costs are for overdrawing an account—all without a prescribed opt-out notice.

Giving customers a better deal cannot be considered injury. In the case of overdraft accommodation, charging someone the same (or lower) fee for *honoring* a check (or ACH or recurring debit card charge) as for *refusing payment* when funds are not sufficient, cannot be classified as an injury to the customer. To do so turns the notion of injury on its head. In the case of overdraft accommodation the monetary impact of the fee is less than the combined charge of an NSF charge for refusing payment and the likely additional merchant charge for writing a bad check—and that does not include the costs involved if the refused payment is proffered by the merchant a second or third time with similar results. It is not an injury if the

[3] *In re Orkin Exterminating Co.,* 108 F.T.C. 263 (1986), *aff'd, Orkin Exterminating Co. V. FTC,* 849 F.2d 1354 (11th Cir. 1988).

consumer's behavior is assessed less money in total than it would be assessed in the absence of the practice—in this case discretionary risk-based accommodation of an overdraft by check, ACH or recurring debit card charge. Such an overdraft fee is neither coercive nor injurious. Rather, it is the price for a bank accommodation—for a bank taking a risk when fulfilling a customer's payment instruction, rather than denying a transaction. In other words, overdraft accommodation is a benefit, not an injury.

Although the same net difference in charges does not currently exist for the payment of debit card present point-of-sale (POS) or ATM transactions, the fee assessed continues to be a known previously disclosed amount. Even if one concludes that there is a monetary harm in these limited instances, this distinction in circumstances does not re-cast fees for overdrawn checks, ACH or recurring debit card payments as injuries. The agencies should not fudge the analysis when establishing precedent that will become the yardstick of future cases yet unimagined.

At this point it must be concluded at a minimum that overdraft accommodation fees are not injuries under the standards the agencies have established to define unfair practices—and this analytical failure dooms a finding of unfairness with regard to them.

Overdraft accommodation fees are reasonably avoidable.

Under the UDAP unfairness standards adopted by the Board and OTS for this rule-making, the concept of not reasonably avoidable is linked to whether the bank has created an impediment to customer action to avoid an "injury." The Interagency UDAP Guidance states in paraphrase of the FTC Unfairness Statement, "The agencies will not second-guess the wisdom of particular consumer decisions. Instead, the agencies will consider whether ***a bank's behavior*** unreasonably creates or takes advantage of an obstacle to the free exercise of consumer decision-making." (Emphasis added.)

The analysis presented by the agencies claims no bank behavior that creates or takes advantage of an obstacle to customers' abilities to manage their own accounts and to *reasonably* avoid overdrawing them. In fact, the analysis purporting to show that fees are not reasonably avoidable is woefully deficient, citing one example where the "consumer cannot know with any degree of certainty when funds from a deposit or a credit for a returned purchase will be made available" as proof that consumers often lack sufficient information about key aspects of their account. Neither the example, nor the assertion it is meant to illustrate, however, constitutes a bank behavior that "unreasonably creates or takes advantage of an obstacle to the free exercise of consumer decision-making."

Our whole retail banking system relies upon the acknowledgment that people are responsible for managing their own bank accounts and their own financial affairs—and it is not unfair to expect that they do so. Knowing what moneys are in their accounts has always been the responsibility of the accountholders. Furthermore, from the beginning of banking the movement of funds has always meant that there will be a certain amount of uncertainty about what the account balance is at any precise point in time. Indeed, customers are in the best position to know their balance as only they know what transactions they have made, including those that have not yet reached the bank or been processed.

Today, people have more current information and tools than ever before, but the basic challenge remains and the onus on personal responsibility must remain. People know the transactions they have conducted—not the bank that can only find out after the fact. Overdraft accommodation programs have been very popular with our customers; specifically because they offer customers a convenient means of addressing occasional uncertainties in their account balances due either to customer oversight or to the timing of receipts into and payments from their accounts. Rather than being an obstacle to customer choice, overdraft programs are tools to accommodate customer choices.

Although not a Commission document, the paper entitled, "The FTC's Use of Unfairness, Its Rise, Fall and Resurrection," by Howard Beales, III, written when he was FTC Director of the Bureau of Consumer Protection, provides persuasive additional guidance for applying the reasonably avoidable standard: "If consumers could have made a different choice, but did not, the Commission should respect that choice. For example, starting from certain premises, one might argue that fast food or fast cars create significant harms that are not outweighed by countervailing benefits and should be banned. But the concept of reasonable avoidance keeps the Commission from substituting its paternalistic choices for those of informed consumers."

Those who choose to manage their accounts with little or no balance as a cushion take a risk that they will sometimes be wrong either through bad arithmetic or the uncertain presentment of multiple transactions through different channels from a variety of sources. This may result in an "inadvertent" unavailability of funds, but it is precisely for this reason that overdraft accommodation is provided by banks *as a benefit to customers*. Customers can improve the chances of avoiding overdrafts by managing their accounts through a variety of means (see FFIEC brochure). These include keeping careful, up-to-date track of transactions; keeping a "cushion" for occasions when mistakes are made; arranging for the checking account to be linked to a line of credit, savings account, or credit card; or arranging for the bank to send an alert when the balance falls below a set amount or a daily notice showing the balance.

Being able to *reasonably* avoid an injury does not mean being able to *absolutely* avoid and act with perfect knowledge. Millions of people conduct billions of transactions a day without overdrawing their accounts. People go years without incurring an overdraft. Perfection cannot become the standard for what it means to reasonably avoid a fee in the banking business. As we have previously noted, all of the banking agencies joined in publishing a consumer brochure, "Protecting Yourself from Overdraft and Bounced-Check Fees," distributed with a press release that noted "the *best way to avoid* overdraft and bounced-check fees is to manage accounts wisely." It is unreasonable that—without withdrawing the brochure—the agencies can conclude that their own advice on the "best way" to avoid fees is not a reasonable way to avoid fees.

Overdraft fees are also reasonably avoidable by selecting other account packages, electing the use of alternative overdraft protections for which one may qualify or by selecting another bank that offers a more favorable mix of features or prices. Many banks also voluntarily offer an opt-out from their overdraft accommodation services. However, the existence of these alternative options in the market does not change the fundamental fact that overdraft fees are reasonably avoidable by customers applying normal financial prudence—and the occurrence of the inadvertent overdraft is not rebuttal thereof.

It follows that overdraft fees incurred through any channel are reasonably avoidable and their assessment cannot be considered unfair if one is faithful to the FTC standards for exercising UDAP authority.

Overdraft services provide countervailing benefits to consumers and competition that outweigh the costs in fees.

As the Interagency UDAP Guidance states, "…[T]he injury must not be outweighed by any offsetting consumer or competitive benefits that are also produced by the act or practice. Offsetting benefits may include lower prices or a wider availability of products or services. Costs that would be incurred for remedies or measures to prevent the injury are also taken into account in determining whether an act or practice is unfair. These costs may include the costs to the bank in taking preventive measures and the costs to society as a whole of any increased burden and similar matters." As ABA has indicated above, safety and soundness impacts of an institutional or industry nature are also appropriately considered as countervailing benefits.

Bank overdraft accommodation programs are popular with our customers because the benefits outweigh the disadvantages and they are sustainable because people want the bank to recognize that when they overdraw their account they can be trusted to make it right. People want their authorized transactions paid and demonstrate that by expressing their satisfaction when it happens[4]. As a recent survey of 1,000 respondents revealed, 85 percent of customers who overdrew their accounts said they were happy that their bank covered their overdraft. Transaction accounts are at-will arrangements. Customers can change banks at any time for any reason—and do. Banks compete for new customers and to retain existing customers. Losing a customer is costly in terms of the outlay spent on attracting a new customer. A program that on-net harms customers has no longevity because it generates no lasting value for either party.

As previously demonstrated, covering overdrafts is less costly to customers than the alternative of refusing payment and returning items. Paying items rather than returning them helps customers avoid adverse credit experience and fees imposed by

[4] See ABA Overdraft Fee Study, Ipsos U.S. Express Telephone Omnibus, (July 11-13, 2008).

disappointed payment recipients, including merchants, creditors, and the government. If checks are returned, payment recipients may be less willing to accept checks from those customers in the future. For example, some landlords and creditors demand cashiers' checks after a payment has been returned for insufficient funds.

Refusing to cover POS transactions has similar implications for the consumer at the check-out counter. What trust would a merchant have in accepting a check from a customer who has just been refused for a debit card purchase? The merchant already knows the account does not have enough money to cover the purchase in question. (Is the merchant going to believe the customer only exercised a partial opt-out option?) The consequences of a failed payment transaction, together with the impact of the embarrassment of having an item returned or denied should not be under-estimated—especially when an increasing percentage of customers use debit cards as their primary payment method, often carrying no other payment means.

Overdraft fees have their own value in terms of signaling the cost of lax personal account management. After all, people should be encouraged to manage their accounts and not to overdraw them. The overdraft fee is set to discourage overdrafts, while not precluding the ability to complete a transaction made at the customer's instruction at a known and competitive cost. This is a pro-market effect and represents a countervailing benefit.

In this period of market stress, it is even more important to consider the safety and soundness implications of regulatory rule-making. Banks' financial welfare derives from a diversified mix of services and loans. Imposing unnecessary compliance costs impairs bank efficiency and financial strength. Burdening a popular bank service by imposing compliance costs to establish unnecessary new controls, new forms, new procedures and new monitoring will only raise the costs of providing those services without improving most consumers' welfare. In other words, unnecessary regulatory erosion of bank earnings affects financial soundness, conceivably further eroding system safety. This constitutes a significant factor that needs to be weighed in considering countervailing benefits
For these and other reasons described by other commenters, assessing fees for paying overdrafts is a practice with extensive countervailing benefits that outweigh the fees themselves. By the three standard measures of unfairness, overdraft accommodation is not an unfair practice.

Consideration of public policy militates against making overdraft fees unfair.

Although it is incorporated in the Interagency UDAP Guidance as an element of unfairness analysis, the agencies have failed to apply the public policy factor in developing the proposal. According to this Guidance, "Public policy, as established by statute, regulation, or judicial decisions may be considered with all other evidence in determining whether an act or practice is unfair. …. [T]he fact that a particular practice is affirmatively allowed by statute may be considered as evidence that the practice is not unfair. Public policy considerations by themselves, however, will not serve as the primary basis for determining that an act or practice is unfair." The FTC

Unfairness Statement recites this additional guidance: "…[S]tatutes or other sources of public policy may affirmatively allow for a practice that the Commission tentatively views as unfair. The existence of such policies will then give the agency reason to reconsider its assessment of whether the practice is actually injurious in its net effects."

A relevant source of public policy to consider in evaluating whether a bank's handling of overdrafts is unfair is the Uniform Commercial Code (UCC). UCC Section 4-303(b) provides that "items may be accepted, paid, certified, or charged to the indicated account of its customer in any order." Official Comment 7 to the section includes the following observation in support of this payment order discretion: "The drawer has drawn all the checks, the drawer should have funds available to meet ***all*** of them and has no basis for urging one should be paid before another." (Emphasis added.) This official policy pronouncement recognizes that customers are the initiators of account activity and the burden is on them to have available funds. The UDAP Proposal's rationale that a customer cannot know with certainty the funds in its account improperly reverses the assignment of responsibility established by fundamental commercial law to manage one's own funds availability. It is immaterial whether that must be done under conditions of absolute certainty or marginal uncertainty. Accordingly, UCC policy militates against the agency's assertion of unfairness.

Another more direct source of public policy on overdraft practices is the *Overdraft Protection Program Guidance* in similar versions issued separately by OTS and jointly by the other banking agencies. As described previously, this Guidance, accompanied by amendments to Regulation DD, established requirements and best practices that delineated how banks should safely, soundly and compliantly conduct their overdraft accommodation services.

For the past several years, the industry has followed this Guidance and executed its overdraft accommodation services in a compliant manner. None of the supervisory agencies have reported any systemic deficiency in the industry's observance of the Guidance. Yet, despite this record, the agencies have precipitously reversed gears to target overdraft accommodation services. Taking mainstream industry practices endorsed by the agencies a scant three years ago, and labeling them unfair illustrates the inappropriateness of the use of UDAP authority in these circumstances. It is one thing for regulators to conclude that new guidelines or regulatory standards are appropriate going forward; it is quite another to conclude that compliance with earlier standards is now somehow unfair.

Asserting that overdraft accommodation is unfair undermines established federal payments policy.

Section 18(f) of the FTCA expressly recognizes the Board responsibility to exercise its rule-making authority to avoid any serious conflict with essential monetary and payments systems policies of the Board. Although this charge is recited as a limit on the Board's obligation to adopt rules initiated by the FTC, it would be absurd for the Board to ignore this obligation when it, or the other empowered banking agencies, initiate their own rule-making. Similarly, the OTS, in applying the public policy criteria of the standard 4 element test of unfairness, should also consider the payments policy implications of using its UDAP authority.

The Expedited Funds Availability Act and Regulation CC heavily regulate the process by which checks are handled, funds are made available, and consumers are advised thereof. Yet, despite the fact that much of the unfairness argument asserted by the agencies revolves around payment systems and funds availability, there is no consideration of the extensive existing regulatory notice requirements informing customers when funds from their deposits will be available. ABA contends that Regulation CC is the foundation for what customers should expect about the availability of their funds and accordingly, establishes customers' responsibilities to manage their accounts in accordance with that knowledge. Application of a UDAP unfairness rule for overdrafts disrupts this framework by interposing a shift in expectations for customer responsibilities by excusing the role Regulation CC bestows on them to understand the limits of funds availability.

Although the Electronic Funds Transfer Act (EFTA) and Regulation E heavily regulate the process by which electronic payments are executed, and consumers' rights are protected, the agencies have not considered this body of law in developing an opt-out for ATM or POS debit card transactions. ABA contends that using a generic trade practices authority such as UDAP that requires joint agency action to implement a uniform legal standard instead of using the more direct regulatory authority intended to govern electronic transactions ultimately detracts from, and works to the detriment of, the EFTA framework.

ABA believes that both the Board and OTS should reconsider using UDAP to address overdraft practices. From a close reading of the proposal, it is apparent that concerns really revolve around debit card transactions—a purely electronic payment systems issue. Regulation E affords the ability to address all of the relevant debit card concerns and to reach beyond the banks themselves to the merchants that are a necessary part of any effective process. Using UDAP instead of Regulation E undermines the continuity of electronic transactions law and needlessly divides the law that governs such payments into more dispersed authorities that complicate achieving coordinated policy, uniform rules and consistent enforcement.

UDAP AND THE PROPOSALS ON PARTIAL OPT-OUT AND DEBIT HOLDS

ABA contends that the preceding analysis proves that customers are not injured in net affect by mainstream overdraft accommodation practices and in any case can reasonably avoid overdraft fees by engaging in prudent account management consistent with long standing public policy. Accordingly, there is no foundation for the assertion that assessing overdraft fees without an advance or continuing opt out choice or notice is unfair. Without this foundation the proposals on partial opt-out and debit holds under UDAP also fail.

The agencies seek additional comment on aspects of the partial opt-out. First, a rule that only compels an opt-out covering only ATM and POS transactions, if predicated on

UDAP, is still flawed for the reasons recited in the previous analysis. In addition, the technical hurdles that currently exist to implementing such a limited opt-out generate costs that further outweigh the benefits of such a rule.

Even accepting for the sake of argument the proposal's unfairness analysis, a full opt-out eliminates the offense and a partial opt-out cannot be separately compelled. Even if the only unfair practice were assessing fees for accommodating debit/ATM overdrafts without offering opt-out, the bank would not be compelled by UDAP to offer a tailored opt-out instead of a general opt-out of its accommodation practices that encompassed debit/ATM as well as other transactions. A partial opt-out cannot properly be enforced under UDAP because the exercise of partial opt-out is only an election of a discretionary overdraft service and is not a contractual promise to pay overdrawn checks and ACH transactions. Consumers cannot effectively say, "Do not pay my POS, but pay my checks," because they have no right under law to write bad checks and compel the bank to pay them. In other words, UDAP cannot be used to require the provision of overdraft accommodation for checks or ACH under the guise of a partial opt-out of debit transactions.

Currently, banks that allow customers to opt out of having overdrafts paid are only able to provide an opt-out on an "all-or-nothing" basis, that is, within the limits of their systems; overdrafts from all payment channels are returned or denied. While technically, with enough time and money, it may be feasible to allow customers to opt out by payment channel, for the vast majority of banks this is not an easy or inexpensive task. Moreover, it is a regulatory cost that will increase in relative terms for smaller institutions. Indeed, the cost differential could be so significant that smaller institutions will be forced to decline to offer customers overdraft accommodation rather than carry the costs of an expensive multi-option program.

More problematic is that the challenge is not just distinguishing debit card transactions from ACH, but also distinguishing card present POS transactions from recurring payment uses of debit cards. The technical challenges are not matters of simply implementing existing fixes. Because there really is no readily available methodology for offering a partial opt-out that can distinguish between card present POS and scheduled recurring payments that mimic ACH, there is no reasonable horizon that can be projected for achieving compliance with such a requirement. As the Board has recently noted in connection with mortgage practices amendments to Regulation Z, if banks are not provided a reasonable time to make changes to their operations and systems they would incur excessively large expenses that would be passed on to consumers. Conversely, such mandates would cause the bank to cease engaging in the accommodation service altogether thereby depriving the majority of customers who would elect the coverage and the benefits thereof. Such compliance costs that are passed on to consumers are a recognized countervailing factor under the standard unfairness criteria. Therefore, the countervailing compliance costs and implications for service outweigh any limited benefit of a limited POS opt-out for the foreseeable future.

Additional countervailing obstacles arise to making an effective partial opt-out for debit transactions. For example, even under a partial opt-out process, there will still be instances when banks will end up paying debit card transactions that may cause an overdraft. The proposal recognizes two such occasions. But more exist. For example, banks may not be able to avoid overdrafts caused when deposited checks are returned unpaid. In such a case, a customer who has made a deposit and relied on Regulation CC availability rules may spend funds by debit card that ultimately are not collected. This would result in an overdraft that the bank could not have stopped (absent a longer hold.)

Unavoidable overdrafts can also arise when computer systems go down. In these cases, customers often continue to have access to their funds based on an approximation of their prior balance, not on their actual balance. However, when the debit transaction is later presented, there may not be sufficient funds to pay the obligation and an overdraft occurs. These are just a couple of many examples of numerous contingencies that may arise in payment processing that can result in unintended debit overdrafts even though no overdraft accommodation program is in place.

It would be unsafe and unsound for banks to assume these risks of debit card overdrafts without appropriate compensation. Were banks to change their practices to minimize these occasions—such as not permitting the use of debit card when systems go down—customers with adequate funds (i.e., most customers by far) would be unnecessarily denied use of their payment option of choice. Under some circumstances, it may even be necessary to re-design account features or re-price the account bundle to properly manage the bank's risks from overdrafts that arise due to the limitations of the systems. This and similar countervailing effects demonstrate why existing bank overdraft accommodation of debit transactions are not unfair.

The debit holds proposal is fraught with problems. First, it is predicated on circumstances that involve two parties that are not encompassed by the current reach of the proposal—card systems and merchants. These are key players in the debit hold story. In fact, the more one studies the situation, the more one realizes that the supposed problem is on its way to a market solution. Recent changes by Visa to processing options for fuel merchants will reduce the time between authorization and clearance. This process will allow any holds to be cleared within two hours. This fast turnaround will enable many banks to decide not to place a hold on automated fuel dispenser transactions in view of the fact that a final transaction message will be transmitted in a known short time frame thereby minimizing risk exposure.

Second, the complexity of debit holds defies simple solutions and exacerbates the expense of developing alternatives. Numerous exceptions would need to be devised to address the variety of presentation contingencies—and they would all further complicate the operational and compliance challenges of implementation. This reality translates to countervailing compliance costs that outweigh the benefits that might come from implementing changes. Third, the complexity of debit holds practices defies detailed disclosures that customers can readily understand. Rather, the path should be to pursue simplification and encourage merchants (like many hotels have done) to advise patrons that use of debit cards may impact their funds availability earlier than, and beyond the amount of, their final transaction. This could be more readily achieved under Regulation E.

Fourth, the proposal's legal analysis underestimates the countervailing impact on the processing systems banks use when exercising their overdraft accommodation discretion. The agencies claim to "understand that financial institutions charge overdraft fees in part to account for the potential risk the institution may assume if the consumer does not have sufficient funds for a requested transaction [and need] to protect against potential losses due to non-payment," the proposed provision does not adequately address the risk arising from the consumer conducting transactions subsequent to the one that generated the hold and while that hold is outstanding. The agencies fail to recognize that restricting when in the decision-making process banks can charge fees for overdrafts that follow in time those debit card authorizations that generate open holds creates a burdensome and unworkable clearance and fee assessment process.

ABA urges the agencies to withhold issuing any final rule on debit holds to provide time for the market to implement its responses. Then it would be appropriate for the agencies to investigate the resulting operational realities. Should there be a continuing need for proscriptive rules; ABA urges that they be proposed under Regulation E where all the relevant parties can be reached within the scope of a single rule-making.

APPLYING UDAP ANALYSIS TO OVERDRAFTS HAS MULTIPLE DRAWBACKS

Banks generally desire clarity and certainty in their compliance obligations. ABA appreciates the agencies' effort to try to bring greater certainty to the application of UDAP to overdraft accommodation practices. Unfortunately, Section 18(f) UDAP rule-making authority has several disadvantages that can lead to unintended and disruptive policy consequences that undermine its value as a tool for establishing uniform standards. Although the agencies have tried to limit these adverse impacts by crafting rule text that does not declare particular practices to be unfair, the assertions contained in the proposal's supplementary information legal analysis undermine this care.

Litigation and Supervisory Risks. Although Section 18(f) restricts rule-making authority under the FTCA, the banking agencies have no exclusive right of enforcement for UDAP standards. Many state laws empower Attorneys General or private parties to sue banks for unfair business practices and to modify the federal standards as suits their particular jurisdictions and state legal precedent. In other words, full implementation of the proposed rule may still leave banks vulnerable to action by other agencies or individuals if, in promulgating the rule, the banking agencies conclude or assert in justification of the rule that overdraft protection fees are not reasonably avoidable and are not outweighed by countervailing benefits.

At the risk of belaboring the point, it is important to understand that if the Board and OTS articulate a finding, conclusion or authoritative assertion that overdraft protection fees are unfair, then significant litigation and regulatory risk could very possibly be generated not only for future but for current programs that today are in full compliance with regulatory mandates and guidance. For example, if the Board and OTS authoritatively find that applying overdraft protection fees without advance opt-out is unfair, Attorneys General, private litigants and even the other state and federal banking agencies will be able to invoke that conclusion in litigation and supervision—including potentially retroactively—against activities that heretofore have been fully consistent with existent statute and regulatory guidance. Findings or conclusions contained in the rule-making analysis will also be asserted as binding precedent by persons invoking the banking agencies' own complaint processes established under 18(f). In other words, since the proposed rule derives from the same section of the FTCA as compels banking agency consumer complaint offices, the regulatory standards articulated under a rule-making are bound to become the basis of creative assertions of liability in the complaint process.

The analysis contained in the proposal, if allowed to stand, will have a far-reaching effect and serious adverse consequences for a broad range of banking practices (besides overdraft accommodation) that have been industry standards. Moving forward, such action, will operate to chill innovation. The analysis of the reasons why overdraft fees are unfair without advance and continuing opt-out amounts to an argument that absolves customers of their obligation to be financially responsible for managing their transactions. The rationale for concluding that overdraft fees are not reasonably avoidable—the assertion that customers cannot know with certainty their own account balance—threatens, for example, fees associated with customers failing to fulfill their responsibilities to manage their own bank account: e.g., NSF and minimum balance maintenance fees.

Opt-out versus options. The fundamental issue is whether customers have reason to know the consequences of their banking activity. Account agreements recite the conditions on which fees will be assessed for certain actions. Notice provides the requisite level of knowledge to enable consumers to avoid overdraft fees even if the account is subject to the bank's accommodation practices. Experience demonstrates that customers successfully act on that knowledge.

Understanding that point, it is not possible to assert convincingly that an opt-out notice is required to avoid action that as already avoidable. That is to say, no remedy is needed for action that already has remedies and can be avoided under current conditions. There are, therefore, no legal grounds under UDAP for the regulators to prescribe a specific opt-out formula as a remedy.

The remedy that is already available is not just an opt-out *per se*, but rather the availability of other *options* to overdrawing accounts or incurring overdraft fees. That is, even if there are policy reasons to provide individuals with additional choice, opting out is not the only alternative. Establishing a right of opt out creates an affirmative right to alter the features of the account as offered by the bank. There is nothing in the unfairness analysis in the proposed rule that compelling argues for the bank to provide choice through the specific opt-out formula—what possibly could be compelled is a *choice* that does not include overdraft accommodation. The bank can offer a different account bundle of features and fees that excludes accommodation, e.g., a minimum balance account without overdraft protection. Indeed, for safety and soundness reasons, banks should not assume the risks arising from an account that has opted out, such as unknowingly paying overdrafts without appropriate compensation. They should be able to adjust practice, prices, and product designs to reflect the risks and costs of opt-out as well as limitations of the systems.

Requiring opt out as *the* solution to avoiding fees under a UDAP theory threatens to convert bank accounts into government-designed cafeteria plans. While some banks may voluntarily offer opt out, market options that allow the bank to bundle features should not be excluded as a response to overdraft accommodation choice. Indeed, the agencies should make clear there is no unfairness rationale that compels offering opt-out versus offering other accounts that exclude the overdraft accommodation feature. Experience continues to teach us that customer services are best designed through the dynamic market-place interaction of customer demand and bank efforts to design services most effective in meeting customer demand. That dynamic is absent from the regulatory process, which is why regulatory action should refrain from designing services and options for customers.

Other considerations about a regulatorily prescribed opt out. Furthermore, it bears reminding that by definition banks are not required to honor payments ordered by customers for accounts containing insufficient funds. It is an accommodative service provided by banks.

Under a regulatory regime that *prescribes* an opt-out right, failure to opt-out can suggest an entitlement that does not exist in as much as the underlying service is a discretionary accommodation made in the fullness of the bank's risk management authority. On the other hand, it must be understood that even where a customer has opted out of overdraft accommodation, there can be instances where the bank is committed to pay an electronic transaction that happens to settle out of funds. Even if the bank is denied the ability to assess a fee, customers must accept that they are still liable for the overdraft.

Requiring an explicit notice of opt-out at account opening essentially converts all overdraft accommodation services—however minor or informal—into promoted plans—a boundary that prior policy guidance viewed as a trigger exposing banks to more risk and imposing new duties. Eliminating this boundary sends a signal to all banks that there is nothing to lose by promoting formal overdraft protection programs since all the compliance obligations are imposed in either case. This seems a strange result for a proposal intended to de-emphasize overdraft usage.

We do not see how a mandate to offer opt-out repeatedly to a customer can be justified as a prescribed remedy under UDAP. What "opt out" means, in the context of this proposal's analysis, is nothing more than the ability to decline the bank's accommodation in advance or in the future. As long as a customer's ability to decline the accommodation service (e.g., by changing accounts or electing other options) is made known initially, the ability to reasonably avoid fees through opt-out is assured. No more elaborate compliance method is legally necessary.

COMMENT ON TRANSACTION CLEARING PRACTICES

While the UDAP Proposal does not address transaction clearing practices, the agencies solicit comment on the impact of requiring banks to pay smaller dollar items before larger dollar items when received on the same day for purposes of assessing overdraft fees on a customer's account. Under such an approach, the agencies suggest that a bank could use an alternative clearing order, provided that it discloses this option to the customer and the customer affirmatively opts in.

Overdraft fees are calculated based on following clearance systems designed to provide payment processing efficiencies that reflect technical capabilities, customer preferences, and the varied risks banks face for handling different payment channels. These systems, and the clearance order they generate, change as bank risk decisions vary, as technological advances occur, as payment channel mix alters to capture customer usage trends, and as legal liabilities evolve.

Not surprising, the result of such a complex analysis is a variety of approaches within the industry. Many banks clear different items using different rules at different times during the day to take advantage of different processing capabilities. Some electronic items are cleared in real-time, while others are presented in batch by particular networks. There are banks that clear checks after electronic items and others that intersperse them. There are banks that clear checks by check number order; others clear high to low; and still others clear low to high. Transactions conducted at teller lines may clear differently than transactions conducted at ATMs, through the mail, via lockbox, or by ACH. There is simply no one way that banks currently process payments and no one way that could be imposed on all banks that would achieve payment system efficiency. In a world that is moving toward near real-time clearance for transactions conducted in the on-line electronic environment, imposing a rule that requires a payment order based on looking back to the size of all same-day items is a payments disaster that is absolutely contrary to real-time processing. Conducting separate payment processing order calculations for fee purposes amounts to inefficient and burdensome redundancy and for that reason is not commonly found in the industry.

It would be operationally very hard to give individual customers the right to alter the bank's clearance process. In addition, many of these clearance processes are too complex to explain in understandable terms in any customer disclosure.

Moreover, ABA believes that regulatory consideration of payment processing order is a matter that should only be made through the Board's normal payment systems authority. Interposing a UDAP rule on such fundamental payment systems issues would be extremely disruptive and an unjustifiable application of UDAP authority.

PROMOTING RESPONSIBLE OVERDRAFT ACCOMMODATION PRACTICES.

ABA and its members have long been proponents of responsible overdraft accommodation practices. ABA's co-sponsored 24-page *Overdraft Protection: A Guide for Bankers* has been in existence for five years and has been explicitly endorsed by the OTS in its "Guidance on Overdraft Programs."[5] ABA continues to believe that industry best practices and the agencies' Guidance on overdraft protection programs have resulted in fair and responsible overdraft accommodation practices. We believe that the record of the agencies' supervisory experience supports this conclusion. Accordingly, we do not think that rule-making is necessary to maintain or improve on this track record.

There is another lesson relevant to the UDAP proposal on overdraft fees that can be learned from the existing agency Guidance on overdraft programs: effective standards can be established for conducting transactions responsibly by enunciating appropriate practices for mitigating UDAP risk without specifying the definitive unfair being prescriptive in defining practices. For instance, the agency Guidance contains a description of various legal risks and concerns that provide a policy predicate for the enumeration of best practices. This was done by being suggestive without being prescriptive regarding any particular service or practice. Using agency guidance authority rather than formal rule-making preserves both supervisory flexibility and the ability of banks to respond to customer interest, market demands, and changing technologies. Banks can receive instructive directions so that banks can better make risk-based compliance judgments.

The current proposal falls short of such an optimally flexible approach. For example, it is noticeably different from existing Regulation AA language that includes declarative rules that specifically describe particular practices as "unfair" in the rule's text. In contrast, the current proposal recites prescriptive requirements under headings that are labeled "unfair" but that nowhere actually recite in the rule text that a given practice is unfair. Unfortunately from the bank's perspective (supported by past litigation experience), the supplementary information is replete with assertions, findings and conclusions that define existing practices to be in fact unfair. This undoes the preventive rule approach by supplying virtually the same definitive specification that a declarative rule would provide and exposes banks to material litigation and new compliance risks for current mainstream practices.

Although ABA acknowledges that the agencies have limited legal latitude to issue preventive rules under FTCA Section 18(f) and could proceed by additional guidance, we believe the better course is to recognize that UDAP is not the preferred legal or policy basis for regulating overdraft fee practices. Instead, it is better to approach reform by building out from Regulations E, CC, and DD. Such regulatory authorities are, after all, the foundation of existing payment system, deposit account, and consumer protection requirements. Interposing a UDAP regulation that requires joint agency action to reach the same scope is less efficient and presents serious complicating risks not present, or that are more attenuated, under the other regulations.

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[5] The OTS stated as follows: "For savings associations interested in further reading on the subject of best practices, OTS recommends an American Bankers Association publication entitled, "Overdraft Protection: A Guide for Bankers."" 70 Fed. Reg. 8429 (Feb., 18, 2005)

Conclusion

In summary, ABA believes that the Board, the OTS, and the NCUA should proceed cautiously in establishing unfairness rules under their UDAP rule-making authority. UDAP situations are often characterized by case specific facts that defy industry-wide generalization. In exercising their FTCA Section 18(f)(1) rule-making authority, the agencies must be mindful to apply standards that properly consider the unique attributes of the banking sector and take extra care in performing their analysis, because it will have precedent setting application far beyond the particular practices at issue.

Ultimately providing overdraft accommodation is not an injury but a benefit and any associated fees are reasonably avoidable by customers exercising normal care—the kind described in Federal Reserve and Interagency consumer publications. Our customers see real value when the bank stands behind their payment decisions, and they understand that the fee is a source of compensation to the bank for that accommodation. Whether paper or plastic, analog or digital, wired or wireless, customers have the tools to manage their accounts and the responsibility to track their transactions. Bank overdraft accommodation is a convenience that customers who use it value and one that they can avoid if they choose by exercising common care as the vast majority of customers do every day.

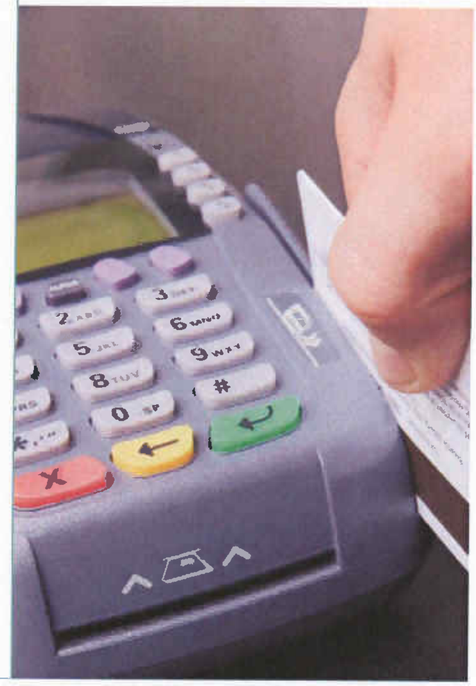
ABA urges the agencies to take special care in considering appropriate standards for this inaugural exercise of banking agency initiated FTCA Section 18(f)(1) rule-making. We ask the agencies to conclude that the banking industry's mainstream overdraft practices are not unfair to customers. We therefore recommend that any new regulatory mandates for consumer protection for debit card transactions be evaluated within the established regulatory framework for electronic transactions, funds availability, and account disclosures.

ABA appreciates the opportunity to provide our comments on this significant proposal and is prepared to provide additional information for your consideration upon request. If you have further questions, please contact Nessa Feddis at (202) 663-5433.

Sincerely,

Ed Yingling
President and CEO

Attachment to ABA comment letter.



Debit Card Danger:

Banks offer little warning and few choices as customers pay a high price for debit card overdrafts

Eric Halperin, Lisa James and Peter Smith
Center for Responsible Lending

January 25, 2007

CENTER FOR RESPONSIBLE LENDING

www.responsiblelending.org

13. Say you made a purchase and did not have enough in your checking account to cover it. Given the following choices, how would you want your bank to handle your overdraft?

N=2140

	Number	Overall Percent	Percent of those who did know	Percent with Preference
Give me an overdraft line of credit with a $5 transfer fee and a 19% annual interest rate (about $1.50 per month for a $100 overdraft)	820	38%	45%	54%
Put the overdraft on my credit card and charge me a $5 fee plus 25% annual interest (about $2 per month for a $100 overdraft)	101	5%	6%	7%
Pay the overdraft for me, charge me a $25 fee, and take the money I owe out of my next deposit	499	23%	27%	33%
Refuse to debit my account for more money than I have in it, return the check unpaid, and charge me a $25 insufficient funds fee	94	4%	5%	6%
I do not have a preference	308	14%	17%	
Don't Know	318	15%		

14. Do you or have you ever received benefits from a government source such as Social Security disability, retirement benefits, veterans' benefits, unemployment, workers compensation, or TANF (Temporary Assistance for Needy Families) cash assistance?

N=2138

	Number	Overall Percent
Yes	814	38%
No	1306	61%
Don't know	18	1%

15. Has your bank ever deducted a portion of these benefits to pay your overdraft fees?

N=814

	Number	Overall Percent	Percent Applicable
Yes	69	8%	13%
No	452	56%	87%
Not Applicable, I was not charged any overdraft fees	256	31%	
Not Applicable, I do not/did not have a bank account	13	2%	
Don't Know	24	3%	